Ketua Pengarah Hasil Dalam Negeri v United Malacca Bhd

HIGH COURT (KUALA LUMPUR) — APPEAL NO WA-14–5–04 OF 2016
AZIZUL AZMI ADNAN J
3 MARCH 2017

Revenue Law — Income tax — Additional assessment — Appellant imposed additional assessment of tax on respondent in respect of late payment charges and retrenchment benefits received by respondent — The appellant imposed penalty on respondent pursuant to s 113(2) of the Income Tax Act 1967 in respect of retrenchment benefits — Whether late payment charges and reimbursement of retrenchment benefits subject to income tax — Income Tax Act 1967 s 113(2) — Land Acquisition Act 1960 s 22

The respondent's land ('the land') had been compulsorily acquired pursuant to s 22 of the Land Acquisition Act 1960 ('the Act'). Dissatisfied with the original compensation amounts awarded by the land administrators and upon litigation, the respondent was awarded additional compensation and late payment charges in respect of the additional compensation. In year of assessment 2009 ('YA2009'), the Land Administrator for Alor Gajah reimbursed the respondent for retrenchment benefits that it had paid to its then-employees ie the estate workers who had been working on the land. Subsequently, the appellant raised a notice of additional assessment for YA2009 by which notice the appellant assessed the respondent to tax in respect of the late payment charges and the retrenchments benefits that had been paid by the land administrator to the respondent. The appellant had also imposed a penalty on the respondent pursuant to s 113(2) of the Income Tax Act 1967 in connection with the retrenchment benefits. The respondent appealed against the decision of the appellant to the Special Commissioners of Income Tax ('SCIT') and the appeal was allowed by the SCIT, hence the present appeal. The issues for court's determination were whether the late payment charges under the Act were subject to income tax; and whether the reimbursement of retrenchment benefits was subject to income tax.

Held, dismissing the appeal with costs:

(1) The late payment charges paid by the land administrators to the respondent under and pursuant to the Act were payments that were capital in nature and were therefore not chargeable to income tax (see para 11).

(2) The reimbursement of retrenchment benefits was not in the nature of income; it was simply a payment for actual expenditure incurred in order

to make the recipient whole. Further, for the appellant to now tax the respondent on the reimbursement of the retrenchment benefits which it had already paid to its then-employees and in respect of which it did not claim for a deduction from its taxable income would in effect amount to a double taxation on the taxpayer. Finally, based on true construction of s 22 of the Act, a reimbursement would only be taxable as income in the hands of a taxpayer if the amount reimbursed had been deducted when determining gross income. In totality, the reimbursement of retrenchment benefits was not subject to income tax (see para 18).

(3) In consequence of the above findings, the penalty on the respondent for its purported failure to bring to tax the retrenchment benefits that it had received in YA2009 had been wrongly imposed (see para 20).

[Bahasa Malaysia summary

Tanah responden ('tanah tersebut') telah diambil alih secara wajib berikutan s 22 Akta Pengambilan Tanah 1960 ('Akta'). Tidak puas hati dengan jumlah pampasan yang diawardkan oleh pentadbir tanah dan atas litigasi, responden diawardkan pampasan tambahan dan caj bayaran lewat berkaitan pampasan tambahan. Dalam tahun taksiran 2009 ('YA2009'), Pentadbir Tanah Alor Gajah membayar balik kepada responden bagi faedah pembuangan kerja yang dibayar olehnya kepada pekerja-pekerjanya pada ketika itu iaitu pekerja-pekerja estet yang telah mengerjakan tanah tersebut. Kemudiannya, perayu membangkitkan notis taksiran tambahan bagi YA2009 notis yang mana perayu mengenakan cukai kepada responden berkaitan caj bayaran lewat dan faedah pembuangan kerja yang telah dibayar oleh pentadbir tanah kepada responden. Perayu juga mengenakan penalti ke atas responden berikutan s 113(2) Akta Cukai Pendapatan 1967 berhubung dengan faedah pembuangan kerja. Responden merayu terhadap keputusan perayu kepada Suruhanjaya Khas Cukai Pendapatan ('SCIT') dan rayuan dibenarkan oleh SCIT, maka rayuan ini. Isu-isu untuk penentuan mahkamah adalah sama ada caj bayaran lewat di bawah Akta adalah tertakluk kepada cukai pendapatan; dan sama ada pembayaran balik faedah pembuangan kerja adalah tertakluk kepada cukai pendapatan.

Diputuskan, menolak rayuan dengan kos:

(1) Caj bayaran lewat yang dibayar oleh pentadbir tanah kepada responden di bawah dan berikutan Akta tersebut adalah bayaran-bayaran yang bersifat modal dan oleh itu tidak dicajkan kepada cukai pendapatan (lihat perenggan 11).

(2) Pembayaran balik faedah pembuangan kerja tidak bersifat pendapatan; ia hanya pembayaran bagi pembelanjaan sebenar yang ditanggung untuk membuat penerima berpuas hati. Selanjutnya, untuk perayu sekarang mengenakan cukai ke atas responden atas pembayaran balik faedah

pembuangan kerja yang mana ia telah bayar kepada pekerja-pekerjanya ketika itu dan berkaitan dengan yang mana tidak dituntutnya bagi pengurangan daripada pendapatan yang boleh dikenakan cukai akan merupakan kepada cukai berganda ke atas pembayar cukai. Akhirnya, berdasarkan atas pentafsiran sebenar terhadap s 22 Akta, pembayaran balik hanya boleh dikenakan cukai kerana pendapatan dipegang oleh pembayar cukai jika jumlah yang dibayar balik telah dikurangkan apabila menentukan pendapatan kasar. Secara keseluruhannya, pembayaran balik faedah pembuangan kerja tidak tertakluk kepada cukai pendapatan (lihat perenggan 18).

(3) Akibat daripada dapatan di atas, penalti ke atas responden bagi kegagalannya yang dimaksudkan untuk mengenakan cukai terhadap faedah pembuangan kerja yang diterimanya bagi YA2009 telah dikenakan secara salah (lihat perenggan 20).]

Notes

For cases on additional assessment, see 10(2) *Mallal's Digest* (5th Ed, 2017 Reissue) paras 2566–2587.

Cases referred to

Ampat Tin Dredging Ltd v Director General of Inland Revenue [1982] 2 MLJ 46 (refd)
Foo Loke Ying & Anor v Television Broadcasts Ltd & Ors [1985] 2 MLJ 35, SC (refd)
Owen v Pook (Inspector of Taxes) [1970] AC 244, HL (refd)
Schulze v Bensted (Surveyor of Taxes) (1915) 7 TC 30, Sc (distd)
Sime UEP v Ketua Pengarah Hasil Dalam Negeri (2002) MSTC 3480 (refd)
The Commissioners of Inland Revenue v Ballantine (1924) 8 TC 595, Sc (refd)
Westminster Bank, Ltd v Riches (1947) 28 TC 159, HL (refd)

Legislation referred to

Income Tax Act 1967 ss 5, 22(2), (2)(ii), 33(1), 113(2), Part III, Chapter 3
Land Acquisition Act 1960 ss 22, 48

Ahmad Isyak bin Mohd Hassan (Ruzaidah Yaacob with him) (Inland Revenue Board) for the appellant.
Anand Raj (Foong Pui Chi and Jess Ngo Hui Zhong with him) (Shearn Delamore & Co) for the respondent.

Azizul Azmi Adnan J:

INTRODUCTION

[1] This was an appeal by the Director General of Inland Revenue against a decision of the Special Commissioners of Income Tax dated 11 July 2014 to allow an appeal by United Malacca Bhd ('the taxpayer') against an assessment made by the Inland Revenue Board. For ease of reference, the office of the Director General of Inland Revenue is referred to in this judgment as 'the Revenue'.

[2] The issues for determination in this appeal relate to the taxability of:

(a) late payment charges received by the taxpayer from the land administrator following a compulsory acquisition of the taxpayer's land; and

(b) the reimbursement of retrenchment benefits paid by the taxpayer to its former employees who had to be made redundant as a consequence of the compulsory acquisition.

Background

[3] Several parcels of land owned by the taxpayer had been compulsorily acquired pursuant to s 22 of the Land Acquisition Act 1960. These acquisitions took place in 1995, 1996 and 2001. The taxpayer objected to amount of compensation awarded by the relevant land administrators, after first having received the original compensation amounts under protest.

[4] Following litigation, the taxpayer was awarded additional compensation as well as late payment charges in respect of the late payment of the additional compensation. These amounts were received by the taxpayer in the years of assessment of 2009, 2010, 2011 and 2012.

[5] In YA2009, the Land Administrator for Alor Gajah reimbursed the taxpayer for retrenchment benefits that it had paid to its then-employees. These employees were estate workers who had been working on the lands that had been compulsorily acquired, and who had to be made redundant in YA1998 and YA1999 as a consequence of the compulsory acquisition.

[6] The Revenue raised a notice of additional assessment for YA2009, by which notice the Revenue assessed the taxpayer to tax in respect of the late payment charges and the retrenchments benefits that had been paid by the land administrator to the taxpayer. The revenue also imposed a penalty on the

taxpayer pursuant to s 113(2) of the Income Tax Act 1967 in connection with the retrenchment benefits.

[7] As a consequence of the position taken by the Revenue, the taxpayer had to bring to tax the late payment charges received in the years of assessment of 2010–2012 in its tax returns for those years.

[8] Dissatisfied with the assessment made and position taken by the Revenue, the taxpayer initiated appeals to the Special Commissioners of Income Tax.

Decision of the Special Commissioners

[9] The Special Commissioners of Income Tax allowed the taxpayer's appeals. The Commissioners found, among others, that:

(a) the late payment charges were capital in nature, and thus were not chargeable to income tax;

(b) the reimbursement of retrenchment benefits would only be regarded as forming part of the gross income of the taxpayer if it had been earlier deducted as an expense; and

(c) as a consequence of the Commissioners' allowing the taxpayer's appeal in relation to the issue of reimbursement of retrenchment benefits, the issue of the penalty no longer arose.

[10] The Revenue appealed to this court against the decision of the Special Commissioners.

WHETHER THE LATE PAYMENT CHARGES UNDER THE LAND ACQUISITION ACT 1960 ARE SUBJECT TO INCOME TAX

[11] I was of the view that the late payment charges paid by the land administrators to the taxpayer under and pursuant to the Land Acquisition Act 1960 were payments that were capital in nature and were therefore not chargeable to income tax. The reasons are as follows:

(a) in my view, the purpose for which late payment charges are imposed is to account for the accretion to capital of the value of the compulsorily acquired land between the time the land was acquired and the time compensation was paid. Therefore, the late payment charges themselves would be capital in nature.

The mere fact that the late payment charges are expressed or calculated as a percentage of the principal value does not of itself mean that those

charges are in the nature of income. The true characterisation of the charges will depend on the nature of the underlying debt, obligation or asset. In *The Commissioners of Inland Revenue v Ballantine* (1924) 8 TC 595, it was held that:

> [A]n interest calculation is a natural and legitimate guide to be used by an arbiter in arriving at what he thinks would be a fair amount. In most cases in which such an allowance is a constituent of award it does not separately appear, but is slumped along with other elements in the gross sum decerned for; but there is nothing to prevent an arbiter, if he thinks it just and reasonable in a particular case, to make the allowance in the form of an actual interest calculation from a past date until the sum fixed as at that date is paid. In all cases, however — whether the allowance is wrapped up in a slump award or is separately stated in the decree — the interest calculation is used *in modum aestimationis* only. The interest is merely in name, for it truly constitutes that part of the compensation decerned for which it is attributable to the fact that the claimant has been kept out of his due for the long period of time. It is not therefore 'interest of money' chargeable under Case II of Schedule D.
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> In *Lee's Trustee v Inland Revenue* [1916] SC 188, Lord Johnston, speaking I think of ordinary judicial decrees, thought that *the assessability of such interest to Income Tax under Case III of Schedule D depended on the character of the debt or obligation in respect of which the decree was pronounced*, and that, if the decree was substantially one of damages, the interest ordered to run on it was just part of the damages, and not therefore chargeable to Income Tax. (Emphasis added.)

In the present case, because the underlying asset was land and was therefore capital in nature in as far as the taxpayer was concerned, the late payment charges would follow the characterisation of the land. It is common knowledge that land, as a finite resource, would in the long run appreciate in value. The late payment charges are intended, as a matter of concept, to compensate the proprietor for this appreciation in the value of the land. In this case, because the taxpayer had been only paid part of the compensation amount at the time the land had been compulsorily acquired, the late payment charges related only to the additional compensation that had not been paid at the time the land was acquired;

(b) this construction is supported by the fact that the relevant provision in the Land Acquisition Act 1960 had been changed from 'interest' to 'late payment charges'.

Section 48 of the Land Acquisition Act 1960, which is the operative provision for the payment of late payment charges, had been amended by the Land Acquisition (Amendment) Act 1997. The effect of the 1997 amendment is illustrated in the marked-up text below:

Section 48 Land Administrator may be required to pay ~~*interest*~~ *late payment charges*.

If the sum which in the opinion of the Court the Land Administrator ought to have awarded as compensation is in excess of the sum which the Land Administrator did award as compensation, the award of the Court may direct that the Land Administrator shall pay ~~*interest*~~ *late payment charges* on such excess at the rate of eight per cent per annum from the date on which the Land Administrator took possession of the land to the date of payment of such excess to the Court or to the person interested.

It is trite law that the court, in construing legislation, must give meaning to the words used in a statute, and cannot treat such words as mere tautology or surplusage. In *Foo Loke Ying & Anor v Television Broadcasts Ltd & Ors* [1985] 2 MLJ 35, the Supreme Court held:

> On the presumption that Parliament does nothing in vain, the court must endeavour to give significance to every word of an enactment, and it is presumed that if a word or phrase appears in a statute, it was put there for a purpose and must not be disregarded. In *Quebec Railway, Light, Heat and Power Co Ltd v Vandry* [1920] AC 662, Lord Sumner in delivering the judgment of the Judicial Committee said (at p 676):
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> > Secondly, there is no reason why the usual rule should not apply to this as to other statutes — namely, that effect must be given, if possible, to all the words used for the legislature is deemed not to waste its words or to say anything in vain.

Accordingly, this court is bound to give meaning to the amendment and to construe the amendment to s 48 of the Land Acquisition Act 1960 as evincing the intention of Parliament for late payment charges to be compensation to a proprietor of lands for the appreciation in value of the land between the time the land was acquired and when the proprietor was actually paid the additional compensation, rather than merely as interest on money to compensate the proprietor for the opportunity cost for having been kept out of funds;

(c) finally, there is also Malaysian authority for the proposition that late payment interest received on property that were sold and which had previously been held as fixed assets (rather than stock in trade) was not business income that was chargeable to income tax.

In *Sime UEP v Ketua Pengarah Hasil Dalam Negeri* (2002) MSTC 3480 the Special Commissioners of Income Tax found that late payment interest on property of a taxpayer held as capital assets constituted capital receipt and was therefore not chargeable with income tax. In a consent judgment entered before the High Court following an appeal in that case, it appeared that the Revenue accepted the position that the late payment interest payable by the purchasers of such properties held as capital assets

would not be subject to income tax. Although such consent judgment does not form a binding authority for this court, it is nonetheless a relevant factor for consideration.

[12] Learned counsel for the Revenue cited a number of cases in support of the contrary position.

[13] In *Schulze v Bensted (Surveyor of Taxes)* (1915) 7 TC 30, the appellant Schulze was a trustee of an estate. He had sued the beneficiaries of a previous trustee (Dun) in connection with the sale of a house, the purchase price for which had not been paid by the purchaser of the house. Dun's beneficiaries were found liable for the principal sum of £1040 with interest at 3 1/2%pa, totalling £461. The issue was whether this interest amount was liable to be assessed for income tax. The Court of Session (Scotland) held that the interest amount in the award of damages constituted 'interest of money' and was hence chargeable to income tax. The Lord President, Lord Strathclyde, in explaining the characterisation of the interest portion of the damages awarded, stated:

> There is a very good working definition of 'interest' to be found in Bell's dictionary. It runs as follows: 'interest of money may be defined to be the creditor's share of the profit which the borrower or debtor is presumed to make from the use of the money. Otherwise stated, it is just recompense to the creditor for being deprived of the use of his money'. Here the trustees on Hugh Lee estate were deprived of the use of this sum of £1040, and if they had had it, presumably it would have yielded them 3 1/2 per cent, and, therefore, as recompense for being deprived of the use of this trust money, they had awarded to them the sum which it would have earned in their hands, if placed in a proper trust investment. That appears to me to make it quite clear that this was interest in the proper sense of the word and not liquidated damages.

[14] Learned counsel for the Revenue sought to rely on this case for the proposition that the late payment charges on the additional compensation awarded pursuant to s 48 of the Land Acquisition Act 1960 should similarly be treated as 'interest of money' and therefore liable to income tax.

[15] In my judgment, *Schulze*'s case can be distinguished on the basis that the underlying payment obligations in that case was a judgment debt due from the former trustee for the taxpayer, and was not a direct claim against a purchaser of capital assets, as was the case in *Sime UEP v Ketua Pengarah Hasil Dalam Negeri*.

[16] The case of *Westminster Bank, Ltd v Riches* (1947) 28 TC 159 is also distinguishable because the interest payable in that case was on profits attained from the sale of shares, which profits would have themselves been subject to income tax. Contrast that with the present situation where it was not disputed

that the principal amount of the compensation payment was capital in nature. (The dispute was only in respect of the characterisation of the late payment charges on the additional compensation awarded by the courts, and not in respect of the chargeability of the additional compensation sum itself.)

[17] The Revenue's first ground for appeal was thus dismissed.

WHETHER REIMBURSEMENT OF RETRENCHMENT BENEFITS IS SUBJECT TO INCOME TAX

[18] In relation to the payment of retrenchment benefits: I found that the reimbursement of such benefits by the land administrator was not subject to income tax for the following reasons:

(a) The reimbursement was not in the nature of income; it was simply a payment for actual expenditure incurred in order to make the recipient whole.

In *Owen v Pook (Inspector of Taxes)* [1970] AC 244, the taxpayer was doctor who held part-time appointments at a hospital located 15 miles away from his practice. On occasions he was required to attend at the hospital, he would be paid travelling expenses for two-thirds of the journey to the hospital (as there was a 10-mile cap on travelling expenses imposed by the hospital's terms of service). These expenses had been included in his assessable income. He appealed to the general commissioners, who upheld his appeal. However, the High Court and the Court of Appeal found for the Inspector of Taxes. On appeal to the House of Lords, Their Lordships allowed the appeal and found, by majority, that the travelling expenses partially reimbursing the taxpayer was not assessable as income. Pearce LJ stated:

> Yet it has been held that he must pay on these reimbursements as if they were income or profit received by him. The point can be underlined by the following example. Suppose that there were some constantly recurring emergency in the most distant part of Pembroke which he was constantly expected to deal with gratuitously and without any extra pay, but he was merely reimbursed for the railway tickets which he had taken to get there and back (or only for two-thirds of his rail tickets so that each time he incurred an actual loss). In that case he would admittedly, if the argument of the Revenue is correct, pay tax on all the reimbursements or partial reimbursements of his railway tickets.
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> Such a situation would obviously be unjust. If it be correct, it is clear that something has gone seriously wrong with the enactments or the case law or both.

The situation in the present case was similar. The taxpayer here was not obtaining 'income' from the land administrator, but was merely being

repaid the amount of an expenditure that had been incurred as a necessary consequence of the compulsory acquisition;

(b) the taxpayer had not claimed the amount as a deduction in the year of assessment in which the payment had been made by the taxpayer. Indeed, I am satisfied that the taxpayer would not have been permitted by the Revenue to deduct the payment of the retrenchment benefit from its taxable income even it had been so minded to claim for a deduction (see the case of *Ampat Tin Dredging Ltd v Director General of Inland Revenue* [1982] 2 MLJ 46, where it was held that retrenchment benefits are not tax deductible under s 33(1) of the Income Tax Act 1967). In such circumstances, to now tax the taxpayer on the reimbursement of the retrenchment benefits (which it had already paid to its then-employees and in respect of which it did not claim for a deduction from its taxable income) would in effect amount to a double taxation on the taxpayer.

In addition, it has to be borne in mind that because the taxpayer paid the retrenchment benefits first (before it was reimbursed by the land administrator), it has incurred an opportunity cost on the value of the amount paid for a period of approximately ten years;

(c) finally, I was of the view that, based on the true construction of s 22(2) of the Income Tax Act 1967, a reimbursement would only be taxable as income in the hands of a taxpayer if the amount reimbursed had been deducted when determining gross income.

Section 5 of the Income Tax Act 1967 sets out the manner in which chargeable income is to be ascertained. The starting point is to ascertain the applicable basis periods and gross income for each such basis period. The methodology for ascertaining gross income is set out in Chapter 3 of Part III of the Act, in which s 22(2) provides:

> (2) Subject to this Act, the gross income of a person from a source of his for the basis period for a year of assessment shall include any sums receivable or deemed to have been received for that basis period in relation to that source by way of —
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> (a) insurance, indemnity, recoupment, recovery, reimbursement or otherwise —
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> (i) where such sums are in respect of the kind of outgoings and expenses deductible in ascertaining the adjusted income of that person from that source; or
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> (ii) under a contract of indemnity; and
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> (b) compensation for loss of income from that source.

On this point, the learned Commissioners had held:

> Daripada peruntukan seksyen ini jelas menunjukkan bahawa *reimbursement* dari 'retrenchment benefit' atau manfaat pemberhentian ini hanya akan dianggap sebagai sebahagian daripada pendapatan kasar Perayu sekiranya ianya ditolak di bawah ACP pada awal dan asalnya ... Mahkamah mendapati di dalam kes ini memandangkan Perayu tidak membuat apa-apa permohonan bagi penolakan apabila bayaran pampasan tersebut dibayar oleh Perayu kepada pekerja-pekerja Perayu pada tahun-tahun taksiran 1998 dan 1999, maka Responden tidak boleh pada masa sekarang mengenakan sebarang cukai terhadap bayaran *reimbursement* tersebut.

I am in complete agreement with the findings of the Special Commissioners that such reimbursement would only become taxable by virtue of s 22(2) if the benefit had been deductible (and had in fact been deducted) for the purposes of determining the taxable income of the tax payer. The key qualification is that contained in sub-para (ii) of the provision, which seeks to treat reimbursements as forming part of the gross income of a taxpayer only where 'such sums are in respect of the kind of outgoings and expenses deductible in ascertaining the adjusted income' of the taxpayer in question.

[19] I accordingly dismissed the Revenue's second ground for appeal.

[20] As I had dismissed the Revenue's appeal in relation to the chargeability of the retrenchment benefits, it follows as a necessary consequence that the penalty on the taxpayer for its purported failure to bring to tax the retrenchment benefits that it had received in YA2009 had been wrongly imposed.

[21] As a consequence, the whole of the Revenue's appeal was dismissed, and the court ordered:

(a) costs to the taxpayer; and

(b) the overpaid taxes to be refunded to the taxpayer.

Appeal dismissed with costs.

Reported by Dzulqarnain Ab Fatar